LIBRARY
SUPREME COURT, U. S.

Office-Supreme Court, U.S.
FILED
APR 15 1965
JOHN F. DAVIS, CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1964

No. 355

BERNARD SUSSER, ET AL.,
Petitioners,

v.

CARVEL CORPORATION, ET AL.,
Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

REPLY BRIEF FOR PETITIONERS

ARNOLD FLEISCHMANN,
ROBERT G. LEVY,
22 Light Street,
Baltimore, Maryland 21202,
Attorneys for Petitioners Modick, McCoy, Phelan, Pierce, Roderis, Giberman, and Pazdro.

Of Counsel:

NYBURG, GOLDMAN & WALTER,
22 Light Street,
Baltimore, Md. 21202.

April 15, 1965.

The Daily Record Co., Baltimore, Md. 21202

IN THE

Supreme Court of the United States

OCTOBER TERM, 1964

No. 355

BERNARD SUSSER, ET AL.,

Petitioners,

v.

CARVEL CORPORATION, ET AL.,

Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

REPLY BRIEF FOR PETITIONERS

ARGUMENT

The purpose of this reply brief is to focus upon the issue which petitioners believe is paramount in this case. It is petitioners' position that Carvel, through its franchise agreements, has imposed a tying arrangement upon its franchise dealers which is *per se* unlawful. This tying arrangement has been systematically and vigorously enforced by Carvel.

The applicant for a Carvel franchise desires to secure a license of the Carvel trademark with the right to operate a retail store displaying the trademark and to sell Carvel soft ice cream and other food products. This applicant further desires to have the benefit of Carvel's expert supervision and guidance in the marketing of soft ice cream

and other commodities. For this valuable license and service, he is willing to pay a royalty to Carvel.

Carvel, however, has conditioned the grant of a license of its trademark, with the right to operate a retail store and the availability of its expertise in the marketing of soft ice cream and other food products, upon much more than the payment of a royalty. Carvel, by means of contractual provisions found in the franchise agreements, further requires that the franchise applicant agree also to purchase from Carvel most of the commissary goods, supplies and equipment which he will need in the day-to-day operation of his retail store. The franchise applicant has but one choice; if he desires to secure the Carvel franchise, he must agree to buy practically all of his commissary items, supplies and equipment from Carvel.

Moreover, the franchise applicant must adhere to this tying arrangement for the duration of his relationship with Carvel. The continued use of the Carvel trademark, the availability of Carvel's expertise and the operation of the Carvel store is conditioned upon the franchise dealer's continued purchases of commissary goods, supplies and equipment from Carvel. If the franchise dealer attempts to purchase these products elsewhere, he will lose his franchise and will be required to surrender his store and equipment to Carvel at a fraction of his substantial cost (See e.g., R. 14, 245-249, 392-393). The franchise dealer will further be restrained from engaging in a similar business for a period of five years within a radius of 25 miles of his store (R. 219). These severe penalties for non-compliance assure Carvel of the dealer's continued purchase of tied-in products.

The Hearing Examiner in his Initial Decision, *In the Matter of Carvel Corporation*, FTC Docket No. 8574, filed

May 25, 1964,* a proceeding similar to the present, summarized Carvel's arrangements with its dealers as follows:

> . . . Carvel's franchise agreements, and its operations under them, effectively prevent its dealers from purchasing freezers, mix, cones and commissary items generally from sources other than Carvel, and impose substantial restraints upon its dealers in purchasing other equipment and items. The restraints are clear, specific and effective. . . .
>
> The Carvel franchise system is founded upon the use of the Carvel name, insignia, designs, procedures, supervision and services. Under the franchise agreement, a fully equipped store, ready to operate, is leased, and its equipment is sold, to the dealer. He is trained in the Carvel method of operation, and is supplied with detailed guides covering the procedures to be followed and the method of producing and dispensing approved items, and he is afforded such supervision and guidance as needed in the operation of the store. The dealer is licensed to use the Carvel name, products and techniques, including copyrights and certain patented equipment, some of which is leased to him.
>
> These are undoubtedly valuable rights and services . . . which may be obtained only upon carefully defined terms and conditions. In return for them, the dealers make substantial initial investments, and undertake the obligations to Carvel discussed above. Upon breach of those obligations, the dealers are subject to the termination of all of their rights under the franchise, the surrender of their stores and equipment at a fraction of their investment, and sharp limitations upon their right to engage in a similar business.
>
> The Carvel franchises are, accordingly, agreements which tie the purchase of equipment, ice cream mix and commissary items to leases and licenses to use the Carvel name, copyrights, patents, products and

* The Commissioners of the Federal Trade Commission heard oral argument on November 18, 1964, on appeals by counsel supporting the complaint and the respondents, but have not issued an opinion as of the date of this brief.

> techniques. They are "tying agreements", and are, therefore, unreasonable if Carvel "has sufficient economic power with respect to the tying product to appreciably restrain free competition in the market for the tied product and a 'not insubstantial' amount of interstate commerce is affected" (¶¶55-58 at pp. 20-21).

The Hearing Examiner, after reviewing economic data pertaining to Carvel's share of the soft ice cream market in the New York metropolitan area, concluded:

> The record in this proceeding convincingly establishes that the exclusive dealing requirements of Carvel's tying agreements with its dealers are associated with a plan and purpose to restrain interstate commerce by isolating from the competitive arena, and channeling to Carvel alone, the entire purchases of the tied products by its dealers. Others are foreclosed from competing with Carvel and selling such products to its dealers, and the dealers, as independent businessmen, are denied the advantages historically attributed to such competition (¶96 at p. 31).

The economic data in the record in the present case amply demonstrates that a substantial market has been foreclosed as a result of the tying arrangement imposed by Carvel on its approximately 400 dealers (R. 19). For example, in 1960, tied-in gross sales by Carvel to its franchise dealers in the five state market were (R. 29):

Mix:	$2,611,324.
Other Ingredients and Supplies:	1,354,599.
Equipment:	494,766.
Total	$4,460,689.

In addition, Carvel realized about $450,000. in royalties on 1,777,650 gallons of mix sold to dealers in the five state market (R. 315-316, 212).*

* Carvel also realizes additional revenues on the lease of stores to its dealers.

Further, a comparison of statistics of the Department of Agriculture pertaining to total gallons of soft ice cream mix produced in the five state area in 1959, with statistics submitted by Carvel for the same year, indicates the following:*

	Department of Agriculture Annual Statistics Bulletin (Exhibit C-10) Total Gallons of Soft Ice Cream Mix Produced in 1959	*Carvel Statistics* (Exhibit C-9) Total Gallons of Soft Ice Cream Mix Produced for Carvel Franchise Dealers in 1959	Carvel's Approximate Percentage of the Soft Ice Cream Mix Market in 1959 (Computed)
Connecticut:	269,000	143,340	55
Massachusetts:	182,000	24,380	13
Pennsylvania:	4,800,000	159,920	3
New Jersey:	2,212,000	347,000	16
New York:	5,416,000	1,190,920	20

The foregoing data clearly indicates that Carvel does enjoy sufficient economic power to restrain appreciably competition in the market for tied-in products.

Because of the unique and desirable characteristics of the Carvel trademark and franchise, the dealer applicant is persuaded initially to agree to purchase most of his commissary and other supplies and equipment from Carvel. The prospective dealer is advised by Carvel that its trademark is one which "practically assures success" (R. 427):

* Carvel Exhibits C-9 (R. 315) C-11 (R. 317) and C-12 (R. 318-319) compare total gallons of *Carvel soft ice cream* mix sold by Carvel in the five state area with the statistics for *total frozen dairy products*, which include hard and soft ice cream, sherbets, ice milk, custard, etc., sold in each of the five states as set forth in the Bulletins of the Department of Agriculture entitled *Production of Manufactured Dairy Products* for the years 1953 to 1959 (admitted in evidence as Carvel Exhibit C-10 (R. 156, T. 3494, 3499)). After 1957, these Bulletins, constituting Exhibit C-10, contain separate gallon figures for soft ice cream. The gallon figures used above are taken from the 1959 Bulletin.

This assertion is strongly buttressed by the statement that the average store displaying the Carvel trademark "grosses $40,000, nets $13,000," while "[s]ome larger units do as much as $80,000" of which amount "the net profit for the unit owner is one-third".* Furthermore, there have been "[n]o business failures in over 21 years in the Carvel chain," which has made over 3,000,000,000 customer services and has thus realized over $300,000,000 in revenues as of 1958 (R. 18, 427). These widely-advertised and desirable features of the Carvel franchise, which are available for an initial investment of approximately $10,500, are sufficient to obtain the dealer's initial acquiesce in the tying arrangement.** After the dealer has executed the franchise agreements, however, the threat of loss of his substantial investment in the franchise is sufficient to compel compliance with the tie-in provisions. The unique and desirable features of the Carvel franchise initially account for Carvel's success in obtaining a tying commitment, while the forfeiture provisions of the agreements assure continued compliance.

Petitioners respectfully submit that Carvel's tying arrangement qualifies as a *per se* violation under either the standard set forth in *Northern Pacific v. United States*, 356 U.S. 1 (1958), which requires a showing of dominance, or the standard enunciated in *United States v. Loew's, Inc.*, 371 U.S. 38 (1962), which provides for an inference of dominance from a tying item's desirability or from uniqueness in its attributes.

Carvel's tying arrangement is further directly responsible for its refusal to permit franchised dealers to sell quality food products customarily sold in competitive stores. A Carvel dealer may not sell Coca-Cola or Hire's

---

* See pages 12-13 of the opinion of DAWSON, D.J., in the fraud suit dated February 7, 1962, which is part of the Record in this case.

** Plaintiffs' Exhibits 22 and 23, admitted into evidence at R. 18, 19.

Root Beer. He may not offer for sale Wise's Potato Chips, Becker's Pretzels, Nabisco's Cookies or Nestle's Hot Chocolate (See e.g. R. 354). Such quality products are obviously compatible with the sale of soft ice cream and would not harm Carvel's reputation, but would mean additional revenues for the dealer. However, since Carvel derives profits from the sale of tied-in products, it naturally will not permit the franchise dealer to offer for sale commodities which would compete, in any way, with those supplied by Carvel. For this reason, a dealer may not sell a quality food product until Carvel has made some arrangement whereby it will derive a profit from the sale of the product to the franchise dealer. At that time, and at that time only, will Carvel amend and supplement the franchise agreement and permit the dealer to purchase the product solely from Carvel (R. 404, 415). It is also made clear to the dealer that he must not attempt to acquire the product elsewhere, for the purchase or sale of an unauthorized product is cause for the forfeiture of his franchise. Thus, the newly-approved item is tied-in to the franchise to operate a Carvel store.

Carvel attempts to justify the tying arrangement embodied in its franchise agreements on the basis that the arrangement is necessary to protect its reputation. Specifically, Carvel complains that it would be impractical to provide specifications to alternative suppliers. This claim is made notwithstanding the fact that Carvel has been able to provide specifications to a number of dairies and cone manufacturers, which supply mix and cones in specified territories to Carvel dealers. The Hearing Examiner, *In the Matter of Carvel Corp., supra*, determined that Carvel could provide specifications to other suppliers and therefore, permit the franchise dealer to purchase supplies in a competitive market. The Examiner concluded that "[t]he

protection of the goodwill and public acceptance of Carvel's products, accordingly, does not necessitate the use of the exclusive tying conditions of Carvel's franchising system", and "Carvel's tradename cannot be used as a device to justify practices which unreasonably restrain trade . . . and respondents concede that the use of secret formulas confers no special immunity for antitrust conduct" (¶106 at p. 34).*

As indicated above, Carvel's argument that it would be impractical to offer specifications to a number of suppliers and thereby, provide a competitive marketplace for the franchise dealers is rebutted by the fact that Carvel does license a number of dairies to supply mix, and a number of cone manufacturers to supply cones to Carvel dealers. The Carvel dealers, however, are required to purchase these products through Carvel and not from the dairy supplying the mix or the manufacturer of the cones. The dealer, because he is tied to Carvel, cannot negotiate price directly with the local dairy which manufactures the mix, although this dairy receives orders directly from the dealer and delivers mix directly to the dealer. This situation applies to suppliers of cones and other products. Carvel's arrangements with the suppliers permit Carvel to fix the price at which the dealer must order these products from the dairy, cone and other suppliers. As the middle-

---

* Lanham Act, Section 33(b) (7), 60 Stat. 427 (1946), as amended 15 U.S.C. Secs. 1051-1127 (Supp. V. 1964) specifically allows as a defense in an infringement action, the fact that plaintiff violated the antitrust laws. The intent of Congress that the trademark licensing provisions would not supersede antitrust proscriptions is clear. See 92 Cong. Rec. 7636, 7872-74 (1946) (remarks of Senator O'Mahoney). "But it is of such great importance to the public of the United States that restraints of trade shall not be permitted, that the Senate insered [sic] this amendment. . . ." Id. at 7873. See also H. R. Rep. 219, 79th Cong. 1st Sess. 3 (1945); S. Rep. No. 1333, 79th Cong., 2d Sess. 3 (1946), and *Quality Control and the Antitrust Laws in Trademark Licensing*, 72 Yale L.J. 1171, 1202 (1963).

man, Carvel assures itself a profit on the transaction, and the supplier is assured a profitable and stable market.

Carvel suppliers knowingly benefit from the tying arrangement imposed by Carvel on its franchise dealers. Thus, Martin Cain, sales manager of Eagle Cone, a respondent herein, candidly acknowledged that its arrangement with Carvel, whereby Eagle supplied all cones to franchise dealers in Massachusetts, Connecticut and New York, in addition to being advantageous to Carvel, "was also advantageous to Eagle because it assured a stable market [guaranteed by the tying arrangement] for it to sell."* Mr. Cain, in complete candor, stated that this stable market "was especially attractive to Eagle because of the fierce competitive nature of the cone industry where orders are given on an 'as-needed' basis." Mr. Cain further observed that Eagle's arrangement with Carvel was "unique in the industry" since "[v]ery few, if any, of Eagle's fifteen major competitors who supply the above described tri-state area have such contracts with their customers" (R. 115). Thus, while Carvel and Eagle enjoy a stable market guaranteed by the tying arrangement, the Carvel dealer is permanently restrained from securing the advantages available to buyers in a "fiercely competitive" market.

Carvel has argued that it is entitled to use tying arrangements in order to protect its reputation. Unlike the franchise dealer, Carvel has no difficulty in distributing specifications, and in securing competitive prices for products which it requires. Carvel would not hesitate to buy from the seller who quotes the lowest price for a product meeting its specifications, and it does not commit itself to buy exclusively from one supplier for any duration. In short,

* Eagle also transacts business in New Jersey and Pennsylvania, and could supply cones in these states to Carvel dealers, but is precluded from doing so by its arrangement with Carvel.

Carvel is not willing to relinquish the benefits to be derived from a competitive market. The threat to Carvel's reputation does not arise until the franchised dealer asks for the same right which Carvel accords itself. Only at this point does it become impractical to make available specifications for products, and to make certain that the specifications are followed.

The record in this case convincingly establishes that the tying arrangement which Carvel imposes upon its dealers is motivated by a desire to isolate the dealers from the marketplace and thus, to channel to Carvel, substantial purchases of tied-in products. This tying arrangement has that effect on competition which has always been of significant concern to this Court. Suppliers are foreclosed from competing with Carvel in selling to its dealers, and the franchised dealers, as independent businessmen, are denied those advantages historically attributed to such competition.

Respectfully submitted,

ARNOLD FLEISCHMANN,
ROBERT G. LEVY,
22 Light Street,
Baltimore, Maryland 21202,
Attorneys for Petitioners Modick, McCoy, Phelan, Pierce, Rodens, Giberman, and Pazdro.

Of Counsel:

NYBURG, GOLDMAN & WALTER,
22 Light Street,
Baltimore, Md. 21202.

April 15, 1965.